



STATE BOARD OF EQUALIZATION STAFF LEGISLATIVE BILL ANALYSIS

DRAFT

Date:	04/01/14	Bill No:	Assembly Bill 1894
Tax Program:	Local Medical Marijuana	Author:	Ammiano
Sponsor:	Author	Code Sections:	RTC Chapter 4 (commencing with Section 7294)
Related Bills:		Effective Date:	01/01/15

This analysis only addresses the provisions that impact the BOE.

BILL SUMMARY

Among other things, this bill authorizes a county to levy a transactions and use tax up to 5% (or a city to levy such a tax up to 2% on medical marijuana or medical marijuana-infused products, subject to current voter approval thresholds.

ANALYSIS

CURRENT LAW

The State Board of Equalization (BOE) administers locally-imposed sales and use taxes under the Bradley-Burns Uniform Local Sales and Use Tax Law and under the Transactions and Use Tax Law, which are provided in separate parts of the Revenue and Taxation Code. By law, cities and counties contract with the BOE to administer the ordinances imposing the local and transactions and use (district) taxes.

The **Bradley-Burns Uniform Local Sales and Use Tax Law**¹ authorizes cities and counties to impose local sales and use tax. This tax rate is currently² fixed at 1% of the sales price of tangible personal property sold at retail in the local jurisdiction, or purchased outside the jurisdiction for use within the jurisdiction. Of this 1%, cities and counties use 0.75% to support general operations. The remaining 0.25% is designated by statute for county transportation purposes, but restricted for road maintenance or the operation of transit systems. The counties receive the 0.25% tax for transportation purposes regardless of whether the sale occurs in a city or in the unincorporated area of a county. In California, all cities and counties impose Bradley-Burns local taxes at the uniform rate of 1%.

The **Transactions and Use Tax Law**³ and the statutes imposing the additional local taxes⁴ authorize cities and counties to impose district taxes under specified conditions. Counties may impose a district tax for general purposes and special purposes at a rate of 0.125%, or multiples of 0.125%, if the ordinance imposing the tax is approved by the required percentage of voters in the county. Cities also may impose a district tax for general purposes and special purposes at a rate of 0.125%, or multiples of 0.125%, if the ordinance imposing the tax is approved by the required percentage of voters in the city. Under these laws, the combined district tax rate imposed within any county cannot

¹ Part 1.5 of Division 2 of the Revenue and Taxation Code (RTC), commencing with Section 7200.

² Section 7203.1 of the RTC.

³ Part 1.6 of Division 2 of the RTC, commencing with Section 7251.

⁴ Part 1.7 of Division 2 of the RTC, commencing with Section 7280.

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exceed 2%⁵ (with the exception of the counties of Alameda, Contra Costa, and Los Angeles⁶).

Counties can also establish a transportation authority to impose district taxes under the Public Utilities Code (PUC). Various statutes under the PUC authorize a county board of supervisors to create an authority within the county or designate a transportation-planning agency to impose a district tax, subject to the applicable voter approval requirement. District taxes imposed under the PUC must conform to the administrative provisions contained in the Transactions and Use Tax Law, including the requirement to contract with the BOE to perform all functions related to the administration and operation of the ordinance.

Currently, all district tax ordinances administered by the BOE have boundaries coterminous with city or county lines. Some districts consist of multiple counties.

PROPOSED LAW

Among other things, this bill would add the Medical Cannabis Regulation and Control Act (Act)⁷ to regulate and control specified medical marijuana activities. The Act would be administered by the Division of Medical Cannabis Regulations and Enforcement, which this bill creates within the Department of Alcoholic Beverage Control.

This bill authorizes⁸ the board of supervisors of any county, or governing body of any city, to levy, increase, or extend a district tax for tangible personal property that is medical marijuana or medical marijuana-infused property upon two-thirds approval by the board of supervisors or city council and either a majority or a two-thirds approval of the voters. The ordinance proposing a tax would establish how the revenues would be expended and, therefore, determine the vote requirement. The district tax imposed upon medical marijuana would conform to the Transactions and Use Tax Law; however, it would not be considered for purposes of determining the combined rate pursuant to RTC Section 7251.1.

Proposed RTC Section 7294.6 provides that, notwithstanding any other law, the combined rate of the county and city medical marijuana tax shall not exceed the rate of 5%.

RTC Section 7295.6 limits the authority of a city to impose a marijuana tax to a rate not to exceed 2%. This section also provides that an ordinance proposing a tax must contain a provision that any person subject to a district tax under a county ordinance shall be entitled to a credit against the payment of taxes due under that ordinance in the amount of district tax due to any city in the county.

IN GENERAL-DISTRICT TAXES

California voters have approved many district taxes in their cities or counties. These district taxes are levied exclusively within the borders of either a county or an incorporated city, with the exception of the Bay Area Rapid Transit District, which is comprised of Alameda, Contra Costa, and San Francisco counties, and the Sonoma-Marín Area Rail Transit District. Cities and counties that levy a tax within their borders are referred to as “districts.”

⁵ RTC Section 7251.1.

⁶ Exceptions authorized through AB 210 (Ch. 194, 2013, Wieckowski) for Alameda County and Contra Costa County and SB 314 (Chapter 785, 2003, Murray) for the Los Angeles Metropolitan Transportation Authority.

⁷ Adds Chapter 18 to Division 9 of the Business and Professions Code, commencing with Section 26000.

⁸ Adds Chapter 4 to Part 1.7 of Division 2 of the RTC, commencing with Section 7294.

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District transactions (sales) taxes are imposed on the sale of tangible personal property in a district. If a retailer is located in a district, his or her sales are generally subject to district sales tax, either when the purchaser picks up the property at the retailer's place of business or when the retailer delivers the property to the purchaser in the district. Retailers located within a district selling and delivering outside the district, generally are not liable for district sales tax in their district; however, they may be required to collect district use tax in the district of delivery (if applicable) on the transaction.

District use tax is imposed on the storage, use, or other consumption of tangible personal property in a district. Retailers generally must report district use tax if they are "engaged in business" within a district. The most common scenarios when retailers are considered "engaged in business" in a district include:

- The retailer maintains, occupies, or uses, permanently or temporarily, directly or indirectly, or through a subsidiary or agent, by whatever name called, any type of office, sales room, warehouse, or other place of business in the district.
- The retailer has any kind of representative operating in the district for the purposes of making sales or deliveries, installing or assembling tangible personal property, or taking orders.
- The retailer receives rentals from a lease of tangible personal property located in the district.
- The retailer is a retailer of vehicles or undocumented vessels which will be registered, or aircraft which will be licensed, in a district.

A retailer "engaged in business" in a district generally is required to collect and report district use tax on a sale when it ships or delivers the property into the district or participates in making the sale of the property within the district. The following example illustrates when retailers should collect and report district use tax:

A retailer in Sacramento County makes a taxable sale of property that it delivers to the purchaser in the City of Concord in Contra Costa County, who will use the property there. Even though the sale is subject to the state sales tax, the sale is not subject to the Sacramento County district sales tax because the property was required to be delivered pursuant to the contract of sale outside the county. However, use of the property in Concord makes the sale subject to the applicable district use tax in Concord and Contra Costa County. If the retailer is "engaged in business" in Concord and ships or delivers the property to the Concord location, he or she is responsible for collecting and reporting district use taxes applicable in the City of Concord and in Contra Costa County. Conversely, if the retailer is not engaged in business anywhere in Contra Costa County, the retailer is not responsible for collecting any district use tax.

DISTRICT TAXES CURRENTLY ADMINISTERED BY THE BOE

Beginning April 1, 2014, there will be 178 local jurisdictions (city, county, and special purpose entity) imposing a district tax for general or specific purposes. Of the 178 jurisdictions, 44 are county-imposed taxes and 134 are city-imposed taxes. Of the 44 county-imposed taxes, 30 are imposed for transportation purposes.

District taxes increase the tax rate within a city or county because the district tax rate is added to the combined state and local (Bradley-Burns local tax) tax rate of 7.50%. As stated above, subject to certain exceptions, the maximum combined rate of district taxes imposed in any county cannot exceed 2%. Each city district tax counts separately

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against the 2% maximum. For example, if a county imposes district taxes totaling 1.50%, each city within that county can only impose district taxes up to a maximum of 0.50%.

Currently, district tax rates vary from 0.10%⁹ to 1%. The combined state, local, and district tax rates range from 7.50 to 10%. Some jurisdictions impose no district taxes, while others, such as the cities of La Mirada, Pico Rivera, and South Gate located in Los Angeles County have total district taxes greater than 2% because they are subject to the specific exception discussed above. A listing of the district taxes, rates, and effective dates is available on the BOE's [website](#).

BACKGROUND

Medical Marijuana Sellers – Sales Tax. In 1996 California voters passed Proposition 215, also known as the Compassionate Use Act of 1996, which allows patients and their primary caregivers to cultivate or possess marijuana for personal medical treatment with the recommendation of a physician, as specified.

In 2003, Senate Bill 420 (Ch. 875, Vasconcellos, Stats. 2003) was enacted to establish statewide guidelines for Proposition 215 enforcement. In particular, SB 420 clarified that nonprofit distribution is allowed in certain cases for patient cultivation cooperatives, small-scale caregiver gardeners, and dispensing collectives. However, despite the fact that numerous medical marijuana dispensaries are currently in business in California, the sale of medical cannabis is illegal under federal law.

The sale of medical marijuana¹⁰ has always been considered taxable. The BOE issues seller's permits to those medical marijuana sellers that apply and will issue seller's permits to any other sellers making unlawful sales.

In 2007, as part of the BOE's education outreach efforts, a special notice was mailed to California sellers of medical marijuana to clarify the application of tax to sales of medical marijuana and the requirement that they must hold a seller's permit.

LEGISLATIVE HISTORY

[Assembly Bill 2312](#) (Ammiano, 2012) was similar to this bill and also authorized a county to levy a transactions and use tax up to 5% (or a city to levy such a tax up to 2%) on tangible personal property that is medical marijuana or medical marijuana-infused products subject to current voter approval thresholds. The measure was held in the Senate Business, Professions and Economic Development Committee.

COMMENTS

- 1. Sponsor and Purpose.** This bill is sponsored by the author and is intended to provide clarification and comprehensive regulation of medical cannabis in California through a statewide system to afford greater certainty and uniformity regarding the rights and obligations of medical marijuana facilities. It also provides for imposition and enforcement of regulations to prevent unlawful cultivation and the diversion of marijuana to nonmedical use.

⁹ Through specific authority, SB 1187 (Chapter 285, Stats. 2001, Costa) authorizes Fresno County to impose a 0.10% district tax for zoological purposes.

¹⁰ All retail sales, including illegal sales, are subject to tax.

2. Conforming to the Transactions and Use Tax Law. This bill provides that the local district tax imposed upon medical marijuana or medical marijuana-infused products shall conform to the Transactions and Use Tax Law. However, not all of the provisions under the Transactions and Use Tax Law are conducive to the proposed medical marijuana tax. The author may wish to consider amending the bill to incorporate standalone language for these provisions into proposed Chapter 4 (commencing with Section 7294), which include:

- **Operative date.** As written, any new local medical marijuana tax would become operative on the first day of a calendar quarter commencing more than 110 days after the adoption of the ordinance pursuant to RTC Section 7265. However, the 110-day timeframe would not provide the BOE sufficient time to effectively implement the **initial** local medical marijuana tax after the first county and/or city adopts an ordinance imposing such a tax. BOE staff estimates that it would take a minimum of six months to implement the initial medical marijuana program proposed by this bill. In order to provide the BOE with the necessary 6-month lead-time, it is suggested that the bill be amended to provide for a delayed operative date for the first day of the first calendar quarter commencing more than six months after the first ordinance is adopted. This would provide the BOE with sufficient lead-time to successfully implement the initial local medical marijuana tax program.

As other cities and counties adopt a tax, the BOE would need time to notify affected retailers, modify tax returns, develop instructions for BOE staff and affected retailers, and perform minor programming changes. The BOE would need at least one quarter lead time from the date the ordinance is approved by the voters to prepare to administer the medical marijuana tax ordinance. The operative date provided under RTC Section 7265, explained previously, should provide the BOE sufficient time to successfully implement subsequent medical marijuana tax ordinances.

- **Administrative costs.** Three different types of administrative costs associated with the local medical marijuana tax would apply: (1) start-up costs related to the implementation of a new (and distinctly different) tax program, which includes extensive modifications to the BOE's computer system; (2) preparatory costs for subsequent cities and counties adopting a local medical marijuana tax ordinance; and (3) ongoing administrative costs.
 - **Start-up Costs.** The Transactions and Use Tax Law includes provisions for reimbursement to the BOE for preparatory costs (Section 7272) and administrative costs (Section 7273); however, BOE staff has opined that these provisions would not include reimbursement to the BOE for administrative start-up costs. It is not clear how these one-time start-up costs would be funded.
 - **Preparatory Costs.** Preparatory costs include developing procedures, programming for data processing, developing and adopting appropriate regulations, designing and printing forms, developing instructions for BOE staff and taxpayers, and any other necessary preparatory costs. The Transactions and Use Tax Law limits these costs to be paid by a district at \$175,000. It is unknown at this time if the amount specified would sufficiently cover the BOE's actual costs to perform these tasks for a marijuana tax ordinance.

- **Ongoing Administrative Costs.** Section 7273 requires the BOE to charge an amount for its administration of the district tax ordinance of each special taxing jurisdiction. Under this statute, the BOE is required to use a model for allocating its costs that is based on the methodology described in Alternative 4C of the November 2004 report by the BOE entitled “Response to the Supplemental Report of the 2004 Budget Act.” The methodology (referred to as the “modified revenue” model) utilizes the four sales and use tax program elements as reflected in the approved Governor’s Budget. Those elements are Audit, Collections, Registration and Returns.

As noted previously, the proposed local medical marijuana tax differs from the existing transactions and use tax and therefore should not be part of the “modified revenue” model for allocating administrative costs.

In order to avoid any unintended impact on the General Fund, the bill should be amended to incorporate BOE reimbursement provisions specific to the local medical marijuana tax.

3. **Costs may exceed revenues.** The Transactions and Use Tax Law requires local jurisdictions that levy sales and use taxes to contract with the BOE to administer the district tax so that the entity may levy a tax at a low rate and take advantage of the functions performed by the BOE in administering the sales and use tax system as a whole. Therefore, if a city or county passes an ordinance to impose a district tax on the sale of medical marijuana, that local jurisdiction would be required to contract with the BOE to perform functions related to the ordinance. The BOE would incur start-up costs related to the implementation of a new tax program, which would be the same regardless of whether one county, or all 58 counties and 482 cities, adopt an ordinance to impose the new tax. The ongoing costs would vary based on the number of jurisdictions adopting a medical marijuana tax ordinance and other factors.

If the tax rate is set too low and/or only a few cities or counties impose the tax, the BOE administrative costs would be paid from a smaller revenue base. Under these circumstances, it is possible that the revenues generated by the proposed tax may not be sufficient to cover the BOE's preparatory and ongoing administrative costs.

4. **Suggested amendments.** In order to avoid any uncertainties or ambiguities in administering the local medical marijuana tax, the following amendments are suggested.
 - It should be clarified that the credit in Section 7295.6 relates to district taxes imposed by the city under Section 7295, and not a district tax imposed on all sales of tangible personal property (e.g., a tax imposed under Section 7285.5 or Section 7285.9).
 - This bill does not contain definitions for the terms “medical marijuana” and “medical marijuana-infused products.” Precise definitions for these terms should be incorporated into the bill.
5. **Tax could complicate retailers’ records and reporting.** If approved, a district tax would be levied on the sale of medical marijuana or medical marijuana-infused products. As previously stated, retail sales of medical marijuana and medical marijuana-infused products are already subject to sales tax (including applicable district tax(es)) to the same extent as any other retail sale of tangible personal

property. Accordingly, medical marijuana retailers would be burdened with additional record keeping and the need to segregate medical marijuana transactions in order to report the correct amount of sales and use tax, any current applicable district taxes, and any local marijuana taxes. These segregations have the possibility of increasing reporting errors and confusion.

- 6. Medical marijuana is not a prescription medicine.** RTC Section 6369 of the Sales and Use Tax Law exempts retail sales of medicines, as defined, under certain conditions, including when furnished by a health facility for patient treatment pursuant to the order of a certificated physician, or when prescribed by a certificated physician and dispensed on a prescription filled by a registered pharmacist in accordance with law. Medical marijuana dispensaries generally do not meet the definition of health care facilities provided in that section, nor, generally, are they registered pharmacists. As such, sales of medical marijuana by dispensaries and primary caregivers do not qualify for the Section 6369 exemption, whether or not the purchasers possess a medical marijuana identification card.

COST ESTIMATE

This bill does not increase administrative costs to the BOE because it only authorizes local jurisdictions to impose a higher amount of tax. Voter approval would be required before any tax is levied pursuant to these provisions.

If a city or county adopts an ordinance to levy the tax, the city or county would be required to contract with the BOE to perform all functions related to the ordinance, and reimburse the agency its administrative costs as well as the costs for the BOE's services in administering the ordinance. Costs for preparation and administration of this tax would likely be higher than other district taxes the BOE administers, since the proposed tax is unlike other district taxes.

To the extent that more medical marijuana tax measures are approved by local voters, the BOE will need additional resources to administer the new taxes. The BOE will utilize the normal budget change proposal process to obtain the necessary funding when the number of newly approved measures requires additional staff to administer the workload.

REVENUE ESTIMATE

The bill does not include a specific tax rate, thus a revenue estimate cannot be prepared. The medical marijuana tax revenue is limited to the local agencies that impose a special tax and is dependent on the rate at which the special tax is established.

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